

Taxation of Adult Dependent Insurance Benefits

Without action by the Legislature this fall, a major hassle for state businesses and a new state-imposed pay cut for some employees will take effect soon.

BACKGROUND

Wisconsin adopted an insurance mandate in 2009 to provide coverage to adult dependent children up to age 27 who were otherwise uninsured. When the mandate was adopted, the imputed income associated with this coverage was made subject to the state income tax.

When the federal government adopted the Patient Protection and Affordable Care Act in 2010, a similar federal mandate was established for coverage up to age 26. However, the value of an adult dependent child's insurance coverage was exempted from federal taxation.

Unlike other states, Wisconsin has not taken action to avoid applying the state income tax to these benefits. Wisconsin is now the only state in the nation to tax this coverage.

THE CHALLENGES

By requiring the taxation of the value of adult dependent child insurance coverage, both employers and employees face challenges.

First, employers must determine the value of providing these benefits to the employees whose children receive them. This is easier said than done. When state officials attempted to lay out guidelines for determining this figure, here is what they issued:

"The fair market value of the adult child's health coverage is determined by the employer and insurance provider. Contact your employer for further information. The Department of Revenue cannot determine the fair market value of the coverage."

Without clear direction from the state, employers are scrambling to determine how to best report the taxable value of this coverage. The polling of employees and determination of the taxable value are a substantial incremental expense to employers.

Second, employees whose children receive these insurance benefits will have an out-of-pocket cost assessed to them this fall. By the holiday season, employers will be forced to withhold a greater portion of the impacted employees' paychecks to cover the cost of taxing these benefits.

THE SOLUTION

To avoid these challenges, the Legislature should act during its Fall 2011 session to remove this tax. Representative Pat Strachota and Senator Van Wanggaard have drafted legislation that will favorably resolve this issue, Assembly Bill 277 and Senate Bill 203.

As part of the Governor's "Back to Work" Special Session, AB 277 and SB 203 will repeal this tax, ease the cost of doing business in Wisconsin, and prevent employees from taking a pay cut because this area of state tax law has not yet been federalized.



WMC
WISCONSIN'S BUSINESS VOICE

For more information contact Jason Culotta, WMC Director of Tax & Transportation Policy, (608) 258-3400, jculotta@wmc.org, or visit www.wmc.org.



PAT STRACHOTA

STATE REPRESENTATIVE

Committee on Insurance

AB277

October 6, 2011

Good afternoon. I want to thank the chair and members of the Committee for hearing my testimony today.

AB277 deals with adult dependant imputed income as it relates to receiving health insurance coverage for dependants ages 18 up to 26. The federal government has passed a tax exemption for income which is used to obtain health care coverage for adult dependent children. AB277 gives us as legislators the opportunity to simplify health care reform requirements for employers and consumers by putting our state laws in line with federal laws. This bill federalizes Wisconsin's tax code as it relates to employer payments for adult dependent care coverage retroactively effective for tax year 2011. Wisconsin is the last state to provide this exemption for state income tax purposes for Wisconsin workers.

Many Wisconsin employers and employees would face difficult accounting issues should this bill not be passed. Employers have not been given clear directions from the state on how to properly determine the "fair market value" of these benefits, leaving them scrambling to determine the best way to report the taxable value of their employees' coverage. Employees whose children have been receiving these benefits will have significant out-of-pocket costs imposed upon them if this bill is not passed. Employers will be forced to withhold a greater portion of their employees' paychecks to offset costs of taxing these benefits right before the holidays. This legislation preemptively fixes what could be an administrative nightmare.

AB277 needs to be implemented as soon as possible to stop this end-of-the-year tax dilemma. This bill simplifies Wisconsin businesses' and Wisconsin workers' tax obligations.



WISCONSIN STATE ASSEMBLY

STATE REPRESENTATIVE
STEVE DOYLE

94th DISTRICT

REPRESENTATIVE STEVE DOYLE TESTIMONY ON AB 277

Thank you Chairman Petersen.

Assembly Bill 277 is nearly identical to Assembly Bill 213, which I introduced a couple of months ago. I appreciate the opportunity to speak in favor of Rep. Strachota's bill.

Let me explain how I came to introduce my version of this bill. I was contacted earlier this summer by a constituent who was covered by a family health insurance policy through her employer. When her 25 year old daughter lost her job – and her insurance – my constituent simply added her daughter to the existing policy. She found out later that this would trigger a tax liability for her – the parent who provided the insurance, not the daughter who received it.

My constituent's employer contacted their insurance provider to determine how much "income" needed to be imputed to the mother's W-2 for the year. Although the addition of the daughter didn't cost anything for either the parent or the employer, the insurance company figured the value of the daughter's coverage to be what it would cost for the daughter to purchase a single policy. In this case it was nearly \$4000 that would be added to the mother's income for the year.

I contacted several accountants to find out if the value of a single policy is the correct standard to use. And I found out something very interesting. Many accountants advise small companies to simply ignore the law because the Department of Revenue doesn't enforce it. What that means is that some people have to pay the tax and some don't and it mainly depends upon who your employer is. As a lawyer I find this double standard to be troubling. As a parent of an adult child myself, I find it to be unfair.

With likely cutbacks in BadgerCare on the horizon it is more important than ever that we find alternate ways to provide health insurance coverage whenever possible. Taking away the current penalty against some parents who want to cover their adult children is a step in the right direction. I wholeheartedly support Representative Strachota's bill and I urge a quick and favorable vote on it.

Thank you for your consideration.

Wisconsin Association of Health Plans

DATE: October 6, 2011
TO: Members, Assembly Committee on Insurance
RE: Support for AB 277 – Imputed Income for Dependent Coverage

The Wisconsin Association of Health Plans supports AB 277 and commends Representative Strachota and the bill co-sponsors for their efforts to align Wisconsin Statutes with federal tax code by exempting from an employee's taxable income the costs of health insurance coverage for an adult dependent child.

Federal law requires individual and group health plans that offer dependent coverage to continue coverage of adult dependents up to age 26 and exempts the coverage from federal income taxation. This provides another commercial health insurance coverage option for young people who often forgo health insurance coverage. Wisconsin also requires coverage of adult dependents; however, Wisconsin tax code does not exempt the costs of extending adult dependent coverage.

Although Wisconsin tax code is generally consistent with federal tax code, AB 277 is needed to correct a misalignment that has created confusion in the market and may discourage parents from electing adult dependent coverage.

Wisconsin has long been a place with high rates of health insurance coverage and competitive health insurance markets. This is due in part to a sound regulatory environment that both protects consumers and works productively with insurers. The result is lower health insurance premiums than many other states. AB 277 will support this environment by encouraging coverage for adult dependents.

The Wisconsin Association of Health Plans encourages committee members to support AB 277.

The Wisconsin Association of Health Plans represents 17 health plans and their affiliated organizations.

Anthem Blue Cross and Blue Shield • Arise Health Plan • Children's Community Health Plan, Inc. • Dean Health Plan • Group Health Cooperative of Eau Claire • Group Health Cooperative of South Central Wisconsin • Gundersen Lutheran Health Plan • Health Tradition Health Plan • Humana • Independent Care Health Plan • MercyCare Health Plans • Molina Healthcare of Wisconsin • Network Health Plan • Physicians Plus Insurance Corp. • Security Health Plan • Trilogy Health Insurance, Inc. • Unity Health Plans Insurance Corp.

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